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Banking Law Alert

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Cuomo v. Clearing House Association
Supreme Court Holds Invalid the OCC's Prohibition of State Enforcement of Applicable State Laws; States May Bring Judicial Enforcement Actions Against National Banks

In a ruling that surprised many, on June 29, 2009, the U.S. Supreme Court reversed the Court of Appeals for the Second Circuit and held that the Office of the Comptroller of the Currency's ("OCC") regulation preempting state law enforcement of applicable state laws against national banks to be invalid as far as a state's prosecution of enforcement actions against national banks. *Cuomo v. Clearing House Association, L.L.C., Et. Al.*, 557 U.S. ____ , Slip. Op. No. 08-453 (2009). In doing so, the Court made a distinction between a sovereign's "visitorial powers" and its power to enforce the law, and ruled that the National Bank Act's ("NBA") prohibition on "visitorial powers" does not prohibit "ordinary enforcement of state law." However, such enforcement is limited to enforcement pursuant to filing suit in a court of law, and does not extend to the state's investigation of national banks other than pursuant to a lawsuit, such as issuing subpoenas for information to national banks without court approval.

The *Cuomo* case resulted from the efforts, beginning in 2005, of the New York Attorney General's (then Elliot Spitzer, currently Andrew Cuomo) attempts to investigate certain national banks for potential violations of anti-discrimination laws based on purported racial disparities apparent in data the banks made public pursuant to the federal Home

Mortgage Disclosure Act.[1] In that regard, the Attorney General sent letters to national banks "in lieu of subpoena" requesting that they provide certain non-public information about their lending practices.

The OCC sued to enjoin the Attorney General's investigative and enforcement efforts as an unlawful exercise of visitorial powers under the NBA and the OCC's regulation interpreting the NBA's visitorial powers provision. The Clearing House Association, a consortium of national banks, filed a similar suit. The Attorney General's position, among other things, was that the OCC's regulation should be set aside as unlawful and that his investigation was not a prohibited exercise of visitorial powers under the NBA.

Section 484(a) of the NBA provides that that "[n]o national bank shall be subject to any visitorial powers except as shall be authorized by Federal law, vested in the courts of justice or such as shall be, or have been exercised or directed by Congress or by either House thereof or by any committee of Congress or of either House duly authorized." [2]

The OCC's regulation interpreting Section 484(a)'s prohibition on visitorial powers provides that such prohibited visitorial powers include, among others, "[e]nforcing compliance with any applicable federal or state laws concerning" "activities authorized or permitted pursuant to federal banking law."[3] The regulation specifically provides that, other than as provided therein, "[o]nly the OCC or an authorized representative of the OCC may exercise visitorial powers with respect to national banks" and that "[s]tate officials may not … prosecut[e] enforcement actions, except in limited circumstances authorized by federal law."

[1] While the original investigation apparently involved federal and state anti-discrimination laws, the parties focused on the state's ability to enforce applicable state laws in the proceedings before the Supreme Court.
[2] 12 U.S.C § 484(a).
[3] 12 C.F.R. § 7.4000(a).

The district court deferred to the OCC's interpretation of Section 484(a) pursuant to the Supreme Court's guidance in *Chevron U.S.A., Inc. v. Natural Res. Def. Council*, 467 U.S. 837 (1984),[4] and enjoined the Attorney General from enforcing state fair-lending laws through demands for records and judicial proceedings. *Office of the Comptroller of the Currency v. Spitz*er, 396 F. Supp. 2d 383 (S.D.N.Y. 2005). The Court of Appeals for the Second Circuit affirmed. The Supreme Court affirmed the injunction with respect to demands for records but vacated the injunction with respect to enforcement via judicial proceeding.

Under the framework set forth in *Chevron U.S.A. Inc., v. Natural Resources Defense Council*, 467 U.S. 837 (1984), courts defer to an agency's reasonable interpretation of a statute it is charged with administering. The question at issue then, according to the Court, was "whether the [OCC's] regulation purporting to pre-empt state law enforcement can be upheld as a reasonable interpretation of" the NBA. The Court found that, despite some ambiguity as to the meaning of "visitorial powers," "[e]vidence from the time of the statute's enforcement, a long line of [its] own cases, and application of normal principles of construction to" the NBA make clear the OCC's regulation could not be so upheld.

The Court first turned to the historical meaning of the term "visitorial powers," finding that the term "visitation" when the NBA was enacted in 1864 was understood to refer to the government's act of looking into a corporation's affairs or the act of a supervising officer who visits to examine the manner in which the corporation conducts its business and to enforce the corporation's compliance with applicable laws. With respect to caselaw, the Court discussed several of its cases in this area and stated that its cases have always "understood 'visitation' as [the] right to oversee corporate affairs, quite separate

[4] As explained by the second circuit, under *Chevron* if Congress has spoken directly to the question at issue, then the courts and the agency must comply with that intent. Otherwise, the court asks whether the agency's interpretation is "based on a permissible construction of the statute" and if so, defer to such agency interpretation.

form the right to enforce the law." For example, in *First Nat. Bank in St. Louis v. Missouri*, 263 U.S. 640 (1924) ("*St. Louis*"), the Court upheld the right of Missouri's Attorney General to bring suit against a national bank to enforce a state anti-bank-branching law, holding that while only the federal government may "perform visitorial administrative oversight" the power to enforce non-preempted state law "must rest with the [State] and not with" the federal government.

The Court also distinguished its 2007 decision in *Watters v. Wachovia Bank, N.A.*, 550 U.S. 1, which simply held that a state may not exercise a prohibited visitorial power against operating subsidiaries of a national bank when the exercise of such power is clearly prohibited against the bank itself.

Calling "bizarre" the OCC's interpretation of Section 484(a), which does not preempt the applicability of all state laws but provides that states are prohibited from enforcing those laws, the Court stated that reading the prohibited "visitorial powers" to prohibit only state oversight and supervision, as opposed to enforcement, provides a more logical result. Citing *St. Louis*, the Court found that if a state law is applicable to national banks, then state enforcement of such law is a necessary result.

The Court further held that Section 484(a)'s carve out for state powers "vested in the courts of justice" also demands this result, since "[i]ts only conceivable purpose is to preserve normal civil and criminal lawsuits." Further, "[i]f a State chooses to pursue enforcement of its laws in court, then it is not exercising its power of visitation and will be treated like a litigant." As a result, according to the Court there is a clear distinction between visitation and law enforcement.

Thus, the Court held that the NBA's reference to "visitorial powers" refers solely to supervisory powers, such as administrative oversight and inspection of books and records on demand. When a state attorney general sues in state court to enforce

applicable state laws, however, he or she "is not acting in the role as sovereign-as-supervisor, bur rather in the role of "sovereign-as-enforcer. Such a lawsuit is not an exercise of 'visitorial powers'" and the OCC's inclusion of prosecuting enforcement actions as a prohibited visitorial power in its implementing regulation was in error.

Therefore, the court vacated the Second Circuit's grant of the injunction against the Attorney General to the extent it prohibited him from bringing judicial actions to enforce applicable state law. However, it affirmed the injunction as it applied to the threatened issuance of executive subpoenas by the Attorney General under New York Executive Law, which permits the issuance of such subpoenas in connection with an investigation of "repeated fraudulent or illegal acts … in the carrying on, conducting or transaction of business." In doing so, the Court stated that the issuance of such subpoenas, unlike the brining of a civil suit or obtaining a court-issued search warrant, "is not the exercise of the power of law enforcement 'vested in the courts of justice'" that is exempt from Section 484(a)'s prohibition on the exercise of visitorial powers. Apparently, then, a state's power to enforce its non-preempted laws is limited to enforcement through the judicial system only, and a state attorney general may not conduct its own investigation outside this context.

President Obama's administration would further extend the states' enforcement power over national banks. On June 17 the U.S. Department of the Treasury issued its white paper entitled *Financial Regulatory Reform, A New Foundation: Rebuilding Financial Supervision and Regulation*, which outlines suggested regulatory reforms aimed at overhauling the nation's financial regulatory system. Among other things, the white paper proposes the creation of a new Consumer Financial Protection Agency ("CFPA") to protect users of credit, savings, payment and other consumer financial products and services. Under Treasury's proposal, states would have the ability to implement regulations that are more stringent than the CFPA's, and would have the authority to enforce those laws as well as the CFPA's regulations with respect to national banks

operating in their states "subject to appropriate arrangements with [federal] prudential regulators." While the regulatory reform proposal does not discuss how states will be permitted to enforce laws against national banks, we suspect that the Obama administration contemplates a broader enforcement power than that provided by the holding in the *Cuomo* case, including investigations into compliance by national banks outside of the judicial enforcement context. In any case, the regulatory reform proposal would at least expand the enforcement powers of states against national banks to applicable *federal* laws – those promulgated by the CFPA, a power that they do not have today.

Despite the fact that the OCC's regulation prohibiting the state's exercise of visitorial powers over a national bank did not technically preempt application of state banking law to national banks, the OCC's regulation prohibiting state enforcement of such laws generally made such preemption a practical result. We expect further guidance and litigation with respect to national banks being subject to the enforcement authority of 50 separate state agencies. We believe that the *Cuomo* decision, along with the Obama administration's proposed abolishment of the national thrift charter and further narrowing of the preemption doctrine, is likely to lead to an increase in banks that choose a state charter over a national one.
